



December 25, 2014

Client Update - New ISS Proxy Voting Guidelines for Israeli Market – 2014-2015 Benchmark Policy Recommendations

Further to our previous communications in this respect, we would like to shed some more light on the new proxy voting guidelines recently adopted by the ISS (the "**New Guidelines**"), which for the first time, specifically address the Israeli market. The New Guidelines have become effective as of December 1, 2014. Prior to the adoption of the New Guidelines, the Israeli market was subject to the general EMEA Proxy Voting Guidelines (the "**Former Guidelines**"). This client update addresses two new provisions set under the New Guidelines and also reviews some existing provisions that are often overlooked.

Equity Based Compensation

Probably the most notable change included in the New Guidelines relates to equity based compensation, setting a new standard for evaluating the maximum issuance of equity compensation permitted by the ISS. While the Former Guidelines addressed only the single parameter of dilution; setting a cap of 10% of the company's fully diluted shares; the new restrictions are comprised of two different parameters:

1. The total percentage of dilution; and
2. The three year average "Burn Rate".

The New Guidelines use both parameters to offer companies a possible tradeoff:

1. If its 3 year average "Burn Rate" exceeds 1% of the total shares outstanding, then such company may not exceed a total dilution level of 10% (i.e. such companies will remain subject to the existing standards);
2. If its 3 year average "Burn Rate" does not exceeds 1%, then its total dilution level can be as high as 15%; (note that this may be useful, for example, for companies which have encountered a reduction in their share value and accordingly have a large amount of equity that is outstanding as it is "out of the money"; or for companies that usually only grant a small percentage of equity each year but have large evergreen plans).

The annual "Burn Rate" is calculated by the ISS as follows:

The average three year "Burn Rate" will be determined by repeating the following process for each of the previous fiscal years, with each year being given equal weight:

$$\text{(Equity Granted in Year X)} / \text{(Total Shares Outstanding at the End of Year X)}$$

For example, the applicable "Burn Rate" with respect to 2015 grants will be calculated by applying the above calculation to each of the years 2012, 2013 and 2014, and then finding the three year average during such years.

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Audit Committee Members

The guidelines set forth the already existing ISS policy, of opposing audit committee members that are deemed by the ISS to be "non-independent". This will i.e. mean that in the ISS will oppose re-election of directors who serve as members of the audit committee that the ISS deems to be non-independent.

Additional Highlighted Issues

In addition to the above new policies that have been addressed in the new guidelines, we would also like to highlight some general issues that we believe are important:

Re-election of Directors Approving "Problematic Transactions" - The ISS may oppose re-election of directors that were involved in related party transactions that were not put to a shareholder vote and that the ISS deems to be "problematic".

Independent Directors - The guidelines provide extensive criteria with respect to who may be deemed a non-independent director, imposing in some cases, restrictions that are even more constraining than those already set under Israeli law.

M&A - While fairness opinions may provide an initial starting point for assessing the reasonableness of a valuation set for a certain M&A transaction, the ISS places a strong emphasis on the offer premium, market reaction, strategic rationale and whether related parties have any special interests.

A copy of the New Guidelines can be found at the following link - <http://www.issgovernance.com/file/policy/israel-2014-2015-policy.pdf>

We would be happy to assist you with any questions or clarifications you may have with respect to this Client Update.

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